

**EXHIBIT H**

1 UNITED STATES DISTRICT COURT  
2 SOUTHERN DISTRICT OF NEW YORK  
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3 SECURITIES INVESTOR PROTECTION  
4 CORPORATION,

Plaintiff,

v.

12 MC 115 (JSR)

6 BERNARD L. MADOFF INVESTMENT  
7 SECURITIES, LLC,

8 Defendant.  
9

-----x  
10 In re:

11 MADOFF SECURITIES  
12 -----x

13 August 20, 2012  
14 4:10 p.m.

15 Before:

16 HON. JED S. RAKOFF

District Judge

17 APPEARANCES

18 BAKER HOSTETLER  
19 Attorneys for Trustee  
20 BY: OREN J. WARSHAVSKY  
TATIANA MARKEL

21 YOUNG CONAWAY STARGATT & TAYLOR, LLP  
22 Attorneys for Trustee  
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23 LAUREN T. ATTARD  
24 Securities Investor Protection Corporation  
25

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(Case called)

THE DEPUTY CLERK: Counsel, please state your name for the record.

MR. WARSHAVSKY: Oren Warshavsky of Baker Hostetler for trustee, Irving Picard.

MS. MARKEL: Tatiana Markel, Baker Hostetler, also for Irving Picard, trustee.

MS. ATTARD: Lauren Attard, Securities Investor Protection Corporation.

MR. DUDA: Justin Duda, Young Conaway Stargatt & Taylor, counsel for trustee.

MR. KIRBY: Richard Kirby, K&L Gates, for the defendants.

MS. CLINTON: Laura Clinton, also K&L Gates, for defendants.

MS. LaROSE: Catherine LaRose, also K&L Gates, for defendants.

MR. SCHWED: Greg Schwed, Loeb & Loeb, representing a group of defendants.

MR. WEINTRAUB: William Weintraub, Friedman Kaplan Seiler & Adelman, for the defendants.

MS. JARASHOW: Kizzy Jarashow, Friedman Kaplan Seiler & Adelman, for the defendants.

THE COURT: Good afternoon, everyone.

There is also some folks who are listening in by

1 telephone with the Court's permission. Could they identify  
2 themselves now?

3 (Appearances on telephone given)

4 THE COURT: Thank you.

5 The folks on the phone, if they wanted to be heard  
6 orally at this hearing, had to appear in person, but I have no  
7 problem with their listening in as they requested.

8 All right. Now, as usual, I have been furnished by  
9 the parties with very helpful briefs, and so while I will be  
10 happy to hear from any of the folks here on any issue they want  
11 to be heard on, there is really only one issue that I am  
12 particularly anxious to hear oral argument on, which is the  
13 issue of inter-account transfers.

14 So let me hear first, who wants to speak on that issue  
15 from the defendants?

16 MR. WEINTRAUB: I will, your Honor.

17 May I use the podium?

18 THE COURT: Yes.

19 MR. WEINTRAUB: Good afternoon, your Honor. William  
20 Weintraub of Friedman Kaplan Seiler & Adelman for the  
21 defendants.

22 Your Honor, we have a very simple proposition that is  
23 anchored to the trustee's inability to avoid transfers that  
24 predate the commencement of the liquidation by more than two  
25 years. The proposition simply put is the following. An

1 inter-account transfer, and by that I mean a transfer by one  
2 customer to another that was initiated and completed outside  
3 the two-year reach-back period, we believe is a deposit in the  
4 recipient's account of cash or securities that is the same as,  
5 which should be treated the same as a principal investment.

6 THE COURT: So give me some examples of what these  
7 transfers were, from who to whom?

8 MR. WEINTRAUB: This would be a transfer,  
9 hypothetically, your Honor --

10 THE COURT: I don't want hypothetically. I want real.

11 MR. WEINTRAUB: With respect to my particular client,  
12 your Honor, it was a divorce. The wife had a Madoff customer  
13 account. The husband did not. The wife was going to make the  
14 divorce settlement payment pursuant to a judgment.

15 THE COURT: Of course, we are at a pleading stage so  
16 it is very difficult for the Court to know, but my guess would  
17 have been these were mostly intra-family transfers, yes?

18 MR. WEINTRAUB: I think that they cover the gamut.

19 THE COURT: Do they? Why would someone, for example,  
20 make an inter-account transfer to a total stranger?

21 MR. WEINTRAUB: I couldn't answer that, your Honor,  
22 because that's not --

23 THE COURT: I think my answer is they wouldn't, just  
24 logically.

25 MR. WEINTRAUB: That would make sense, your Honor.

1 Our point is, regardless of the underlying facts, because of  
2 the application of the two-year limitation on clawbacks, that  
3 the trustee cannot avoid and recover transfers outside the  
4 two-year period, it really doesn't make a difference as to why  
5 the inter-account transfer was made. Because as a legal  
6 principle, had the transferor basically just taken out the cash  
7 himself or herself, that transfer would be unavoidable. Had  
8 that same customer taken out that cash and given that cash to  
9 John Doe, for whatever reason, John Doe would not be subject to  
10 a clawback because John Doe --

11 THE COURT: Supposing John Doe was Jane Doe's spouse,  
12 you think that would make a difference?

13 MR. WEINTRAUB: I don't think it would make a  
14 difference, your Honor, because as much as the trustee would  
15 like to avoid transfers that occurred one day before the  
16 commencement of the two-year reach-back period, if a customer  
17 had taken out a million dollars, for whatever reason, that  
18 transfer would not be subject to avoidance. And the fact that  
19 that customer made an inter-account transfer to someone else  
20 should be irrelevant in terms of the legal proposition that the  
21 trustee can't reach back further.

22 THE COURT: I hear you, but I am bothered by your  
23 resort to abstractions. The last I heard the facts drive the  
24 law in this and every other court. So I need to know more. If  
25 these are primarily, hypothetically, transfers say to children,

1 someone gives, in effect, a gift to a child, they take what the  
2 trustee would call the fictitious profits and they distribute  
3 them to their three children and set up new accounts for their  
4 children, that seems to me very different from the kind of  
5 situation you're hypothesizing.

6 MR. WEINTRAUB: Let me answer that in two ways, your  
7 Honor. First, I don't think that it does make a difference  
8 that it's an inter-account transfer to a child because a parent  
9 can do whatever it wants with its money, and the fact that it  
10 hypothetically is a return in excess of principal does not make  
11 a difference if you're outside the two-year period.

12 Now, with respect to my particular client, your Honor,  
13 my client was not a Madoff customer at the beginning of the  
14 two-year period. My client was not a Madoff customer at the  
15 time of the divorce from his wife. His wife was going to make  
16 the payment decreed by the judgment of divorce to the husband  
17 and Mr. Madoff interceded and said, you don't need to do that,  
18 I will basically manage the money for your husband. Let's open  
19 up an account for your husband and make an inter-account  
20 transfer. And that's how my client got caught in this web.  
21 And that was in satisfaction of an antecedent debt from the  
22 wife to the husband, who I also think that when the husband  
23 within the two-year period took his money out of Madoff's  
24 securities, what he was doing was satisfying an antecedent debt  
25 that Madoff Securities had to him because that transfer should



1 be treated as principal.

2 THE COURT: Presumably, you could argue that a  
3 transfer from one former spouse to another former spouse is  
4 about as arm's length as you can get.

5 MR. WEINTRAUB: I am not here just for my client,  
6 although I think my client has very attractive facts. I am  
7 here for all of the defendants who have inter-account  
8 transfers. And again, we believe that there is a universal  
9 principle that should be applicable here, which is because of  
10 the operation of the two-year reach-back period, these  
11 inter-account transfers should be treated as basically a  
12 deposit of principal. It's, in essence, a withdrawal by the  
13 first customer and a transfer of what we believe is an  
14 unavoidable right to payment to the recipient.

15 THE COURT: What case or cases do you think support  
16 that position?

17 MR. WEINTRAUB: Your Honor, we cite cases that talk  
18 about what is a transfer. We referred to the bankruptcy code  
19 definition of transfer. We referred to the bankruptcy code  
20 rule of construction as to when a transfer is made. A transfer  
21 is made when it can no longer be upset by a third party to a  
22 bona fide purchaser. We believe that customer B, the  
23 recipient, is a bona fide purchaser, and there has been what we  
24 call a change in the nature of the investment by virtue of the  
25 inter-account transfer. Because before the inter-account

1 transfer occurred, the right to payment and the right to the  
2 account balance was with customer A. After the transaction is  
3 completed, the control of the right to payment and the right to  
4 the account balance is now with customer B. So you have got  
5 what the cases require as a change in the nature of the  
6 investment.

7 We also relied upon cases that discuss the fact that  
8 you do not need to have an actual deposit of cash to open a  
9 securities account, that a change in the nature of the  
10 investment is all that is sufficient for purposes of  
11 securities --

12 THE COURT: What I am getting at is, I may have missed  
13 it in the briefs of the parties, but I don't think this  
14 specific issue in this kind of context has been the subject of  
15 any case law in the Second Circuit.

16 MR. WEINTRAUB: I think that's right. I believe that  
17 my able adversaries would cite the *Bayou* case and try to say  
18 that the *Bayou* case is dispositive of this, and we think it  
19 isn't. We think *Bayou* involved a completely different issue.  
20 In *Bayou*, investors in what was known as the Bayou Fund were  
21 given the opportunity to redeem, because the fund was shutting  
22 down, or roll the investment over into a new investment in one  
23 of the other Bayou hedge funds. Those customers who took the  
24 roll-over option argued that the entire roll-over amount was a  
25 new investment based upon cases decided under Rule 10b-5 that a

1 change of investment is the equivalent of a new investment.

2 And those investors lost, your Honor, and in the *Bayou* case it  
3 was determined that it was the same investment.

4 THE COURT: Yes. It was the same person.

5 MR. WEINTRAUB: Right. The same person. But in our  
6 case, we have two issues.

7 THE COURT: I will hear from your adversary. The  
8 reason I wanted to hear argument on this matter first is  
9 because it seemed to me, subject to hearing from your  
10 adversary, that this was not an issue that had been addressed  
11 in any prior decision, at least not head on, so to speak.

12 MR. WEINTRAUB: I think that's right. As I was  
13 saying, the two differences with *Bayou* is it's a different  
14 customer, number one. But even more importantly, your Honor,  
15 they did not address the effect of the reach-back period on the  
16 transaction. And here we think that the effect of the two-year  
17 reach-back period is a linchpin of this argument.

18 THE COURT: OK. Thank you very much.

19 Let me hear just on this issue from whoever wants to  
20 speak from the trustee.

21 MR. WARSHAVSKY: Good afternoon, your Honor.

22 In fact, we would cite to the *Bayou* case.

23 THE COURT: Why? As was just pointed out, among other  
24 things, it's a transfer from one person to himself.

25 MR. WARSHAVSKY: Well, that's the case in some of the

1 situations, but the defendants' argument is inter-account  
2 transfers. They didn't specify one person to another.

3 THE COURT: So for the sake of argument, we will  
4 forget about the transfers that are one person to another.  
5 That could easily be distinguished if that was relevant. So  
6 there goes *Bayou*.

7 MR. WARSHAVSKY: That's right.

8 THE COURT: Bye-bye *Bayou*.

9 MR. WARSHAVSKY: Maybe not bye-bye *Bayou* because I  
10 think the reasoning of *Bayou* still stands. And if I can quote  
11 just one sentence from *Bayou*, which is, "In no event is it  
12 appropriate to pile fiction on fiction by deeming these  
13 investors' final Bayou Fund account statements, including  
14 fictitious profits, to be the value of their investments.

15 And that's really what we have here. I know you  
16 haven't always agreed -- if I can take a step back. I know you  
17 haven't always agreed with all the trustee's methodologies and  
18 our arguments, but I think --

19 THE COURT: I think in this particular argument,  
20 you're wrapping yourself in my opinion in *Greiff*.

21 MR. WARSHAVSKY: I sure am. I am wearing it.

22 But I think the one thing we tried to do is maintain  
23 consistency, which is to do a full account reconciliation. It  
24 doesn't penalize innocent investors, but it also doesn't credit  
25 them with fictitious profits. And here, moving that concept

1 forward here in the case -- I don't have the facts of the  
2 particular case that my adversary cited; however, what is  
3 apparent is the original investor, the wife, had gone through  
4 her principal. Under no theory could the amounts that she gave  
5 to her husband be principal. They are fictitious profits. The  
6 husband may have a terrific claim against his wife.

7 THE COURT: I would think the wife undoubtedly thinks  
8 this is poetic justice.

9 Anyway, I understand the point. What they are saying  
10 is that it's, in their view, indistinguishable from if the  
11 transferor had taken the money out, let's say put it in a bank  
12 account, and a year later -- all of this being beyond the  
13 two-year period -- exchanged it for value with the third  
14 person, who then created the account, they are saying you  
15 wouldn't be able to go after that principal investment. Why  
16 are you able to go after this?

17 MR. WARSHAVSKY: That's right. But I think that's a  
18 different argument. The reality is that this person left their  
19 money with Madoff. And ultimately the question is whether or  
20 not value was provided to BLMIS. A transfer in between  
21 accounts does not provide value. And in point of fact, there  
22 are times where the trustee has seen that somebody has  
23 liquidated his or her account and then opened a new account,  
24 and we have treated it separately for just that reason, because  
25 the money did leave and because new money came in and it might

1 be difficult to trace, I don't know if it's possible to trace.  
2 But the point is that value was added. Here none was added.

3 We do go back to the *Greiff* opinion, we do go back to  
4 the statute and look to what the value they're providing. Here  
5 there is none. Here there was fictitious profits moving from  
6 one account to another. And in certain cases it is between  
7 family members. My guess is most of the defendants who would  
8 raise this defense about moving money from account to account  
9 are relatives or -- well, relatives or sometimes we see with  
10 business partners moving money back and forth, but ultimately I  
11 think this case is the zebra. It shows one defendant -- I'm  
12 sorry, Ms. Markel passed me a note. We also see gifts -- I am  
13 not sure I understand. Ultimately what we see is we see  
14 individuals, sometimes for themselves, moving from an IRA to  
15 their savings or to their own discretionary account or vice  
16 versa.

17 The other point that I will add here is, I know your  
18 Honor is not often fond of the absurd results argument.  
19 However, here it really would work an absurd result. Under the  
20 argument my adversary just proffered, what that would mean is  
21 that his client would get a customer claim. If what he is  
22 saying is right, his client put in that value and didn't  
23 withdraw, only withdrew a portion of that, his client is  
24 suddenly entitled to a customer claim. That can't be how we  
25 calculate net equity. And ultimately, not only do I wrap

1 myself in your Honor's *Greiff* opinion, but I always go back to  
2 the Second Circuit opinion, the net investment method, and the  
3 only way to look at each account and to reconcile each account  
4 is to look at cash in, cash out.

5 THE COURT: Before we hear from anyone else, does your  
6 colleague want to tell me what is in her note?

7 MR. WARSHAVSKY: It's a good point from my colleague.  
8 She points out that in many of these instances it's gifts  
9 within the family. So we are not even talking about bona fide  
10 purchasers per value. So we are even beyond this issue.

11 THE COURT: OK. Someone from SIPC wanted to be heard.

12 MS. ATTARD: Just to add to what Mr. Warshavsky said.

13 To the extent that fictitious profits remained in the  
14 Ponzi scheme, it enabled the Ponzi scheme to continue. And as  
15 Judge Posner wrote in *Scholes v. Lehmann*, "A profit is not  
16 offset by anything. It is the residual of income that remains  
17 when costs are netted against revenues." The paying out of  
18 profits to the defendant here was not offset by further  
19 investments to him and conferred no benefit on the corporation  
20 but merely depleted the resources faster. And I think once we  
21 drill down into the actual facts of this case, which is beyond  
22 the scope of a motion to dismiss, we will see that those  
23 fictitious profits should be treated as such.

24 THE COURT: All right. Let me go back then to defense  
25 counsel.

1 MR. WEINTRAUB: Thank you.

2 There was a lot to respond to there, and I will try to  
3 be brief, your Honor.

4 I am going to wrap myself in *Greiff* as well. What the  
5 Court said in *Greiff* was that legitimate expectations of  
6 customers acting in good faith should be fulfilled. And what  
7 happened in this instance, your Honor, in every one of these  
8 inter-account transfer cases, because there is no allegation of  
9 bad faith in any of these complaints, what each one of these  
10 sending customers thought they were doing was implementing a  
11 securities transaction from one account to another, and each  
12 recipient thought that they were receiving a securities  
13 transfer. And each one of those recipients believed that what  
14 they were receiving was something that was basically a  
15 withdrawal from the first customer that was transferred to the  
16 second customer. So by recognizing that these inter-account  
17 withdrawals, if done outside the two-year period, should be  
18 treated as principal, you're giving effect to the reasonable  
19 expectations of innocent investors.

20 We think, your Honor, as we said earlier, because  
21 customer A instructed Madoff Securities to make this  
22 inter-account transfer, that this inter-account transfer  
23 satisfied an obligation of Madoff Securities to customer A. It  
24 was satisfaction of an antecedent debt. The company at that  
25 point was not in bankruptcy. Transfers and obligations may be



1 voidable, but they are not void. And this was a securities  
2 entitlement under state law at the time that this inter-account  
3 transfer occurred, which is more than two years --

4 THE COURT: I guess I am missing the point here.  
5 Wasn't there an offsetting obligation assumed?

6 MR. WEINTRAUB: Exactly, your Honor.

7 THE COURT: So in the global sense, it didn't add  
8 anything of value to Madoff Securities. If anything -- and  
9 this is the part of what the trustee keeps harping on -- by  
10 giving the illusion of Madoff Securities as an ongoing  
11 reputable business, it just enabled the fraud to be  
12 perpetrated. In your specific client's case, it seems to be  
13 typical of that. Your client was all set, if I understand it,  
14 or your client's spouse was all set to take the money out, and  
15 Mr. Madoff, good old Uncle Bernie, said, Why do that, we can do  
16 it all for you? This was just the further perpetration of the  
17 fraud. But I don't see how, in terms of economics, it added or  
18 subtracted anything of value to Madoff Securities.

19 MR. WEINTRAUB: My point, your Honor, was it all  
20 balances out. When the transferor, customer A, makes the  
21 withdrawal, that satisfies an antecedent obligation to customer  
22 A. There is now a corresponding deposit in customer B's  
23 account, which we believe is principal. When customer B takes  
24 that principal out, the question is, does that customer have  
25 the defense under 548(c) for value for payment of an antecedent

1 debt? We believe that it does, because as we said earlier,  
2 your Honor, this withdrawal that was effected through an  
3 inter-account transfer was done outside the two-year period.  
4 It's no different than had customer A taken cash and given it  
5 to customer B. In effect, that's exactly what happened because  
6 it was outside the two-year period.

7 So I would argue, your Honor, that there was value  
8 given to customer B, and Madoff recognized that value because  
9 Madoff wasn't depleted because the cash didn't actually leave.  
10 But at the point in time when you do need to look at what the  
11 effect on the estate is, the real question is, is what was  
12 taken out principal or something in excess of principal? And I  
13 think the two-year reach-back period is the Litmus test for  
14 that.

15 I would just like to make one more point. This is not  
16 a net equity argument. The Second Circuit did not decide this  
17 issue when it decided how you calculate what a particular  
18 customer is entitled to with respect to an unpaid balance.

19 THE COURT: I am shocked you would say that because  
20 the trustee in every argument we have ever had tells me that  
21 that decision decided every question definitively in the  
22 trustee's favor.

23 MR. WEINTRAUB: As you know, that case was very  
24 limited, and that case basically, as far as we are concerned,  
25 held that as between the last-statement method and the

1 cash-in/cash-out method, under the unique facts of this case,  
2 the court selected one method over another because it was only  
3 given two methods. I think the court was pretty clear that  
4 it's not even certain that the court would apply the  
5 cash-in/cash-out method in another case.

6 My point is that the argument that we are making here  
7 has nothing to do with a customer's account balance. We are  
8 not taking a position as to whether or not if less than all of  
9 a transfer that is in excess of principal was left with  
10 customer B, that customer B would have a positive net equity  
11 claim. I think that ship has sailed, your Honor, in terms of  
12 how you calculate a net equity claim. But there is an  
13 insidious consequence of blindly importing the cash in, cash  
14 out net equity formulation to inter-account transfers between  
15 different customers. Cash in, cash out is a lifetime netting  
16 of the specific customer's account history for a specific  
17 account. The purpose of the netting is to establish that  
18 customer's right to his remaining balance, his unpaid balance.  
19 In other words, does the customer have a claim against the fund  
20 of customer property for amounts not yet taken out? The  
21 lifetime netting has nothing to do with avoiding actions. It's  
22 a creature of the claims process and it determines eligibility,  
23 in essence, for the insurance payments. It doesn't want to pay  
24 people out of the \$500,000 for what it considers to be --

25 THE COURT: Let me ask you this. I didn't mean to

1 interrupt, but going back to a point we were discussing  
2 earlier. Do you say that there should be no difference in the  
3 treatment, along the lines you're arguing, between transfers  
4 from one customer to another customer as opposed to transfers  
5 to the same customer just having a different account?

6 MR. WEINTRAUB: No, your Honor, we are not making that  
7 argument. We think that if it's the same individual but a  
8 different account, those accounts, I think, are aggregated as a  
9 matter of law. I am talking about different customers.

10 THE COURT: I just wanted to be sure of that. OK.

11 Just to pursue that, and of course we don't know what  
12 these are, it is one of the problems I am facing in dealing  
13 with this in the abstract. Supposing it's a transfer from one  
14 company wholly owned or substantially controlled by Mr. X to  
15 another company wholly owned or substantially controlled by  
16 Mr. X? Would you treat that as the same customer or would you  
17 treat it as different?

18 MR. WEINTRAUB: I think if they are different  
19 entities, they are different customers. Again, the trustee in  
20 his papers called this money laundering as though --

21 THE COURT: I understood that you rightly took offense  
22 I think at that characterization, but that's not the question I  
23 am asking. It would be very boring if we didn't have at least  
24 one flight of rhetoric from the trustee followed by shouts of  
25 wounded innocence from the defendants. So put all that aside.

1 You're comfortable in taking the position that if it's two  
2 names, two company names, albeit wholly owned by Mr. X, they  
3 should still be treated as the way you would treat  
4 inter-account transfers from one person to a wholly different  
5 person?

6 MR. WEINTRAUB: Yes, your Honor. I think just like in  
7 other areas of law, where the law implies the entity theory, if  
8 the entities are different, they are different. And father and  
9 son are different. Company A and company B are different even  
10 if owned by the same person. So it would be consistent and I  
11 think it's not an unreasonable position if they are completely  
12 different.

13 THE COURT: OK. Anything else?

14 MR. WEINTRAUB: I am not sure I --

15 THE COURT: I cut you off in mid-flight.

16 MR. WEINTRAUB: I am not sure where I was in the  
17 argument, but what the netting does with respect to a specific  
18 customer is lets the trustee basically use unavoidable  
19 transfers because you're looking at an entire history, a  
20 lifetime history of cash in, cash out. So you could be looking  
21 at transfers that were ten years ago, and when you're doing  
22 that netting with respect to a particular customer to get to a  
23 net equity claim, you are basically looking at and using an  
24 unavoidable transfer, a transfer that happened ten years ago,  
25 to negate an investment that may have been made during the

1 two-year period that they net out. And the Second Circuit has  
2 said that you can do that for purposes of determining a  
3 customer's net equity claim.

4 It would seem to me to be wholly inappropriate to take  
5 an ancient transfer that was unavoidable with respect to  
6 customer A and use that transfer to negate the inter-account  
7 transfer made outside the reach-back period to customer B.  
8 You're basically depriving customer B of the benefit of what  
9 was transferred to him based upon something that was not only  
10 ancient, but ancient with respect to a different customer. We  
11 think that's inappropriate and there is no legal principle that  
12 would support doing that.

13 THE COURT: Thank you very much.

14 So now I am happy to hear from anyone else who wants  
15 to be heard on any issue.

16 Go ahead, counsel.

17 MR. KIRBY: Richard Kirby, K&L Gates, on behalf of  
18 defendants.

19 I am going to address two issues today and my  
20 colleague Mr. Schwed will address another issue that was  
21 briefed on these briefs.

22 I am going to discuss the question of whether tort  
23 remedies may be part of the value defense. That's an issue  
24 that was not addressed by this Court in the *Greiff* decision. I  
25 am also going to address the value defense as to inter-account

1 statement obligations that the trustee has not elected to avoid  
2 or have not been avoided or outside the reach-back period.

3 Mr. Schwed will address the value defense as it  
4 applies to new money deposited after the fact.

5 THE COURT: Is there anything you're about to tell me  
6 that's not in your briefs?

7 MR. KIRBY: Yes. There's several points.

8 THE COURT: Why don't you go to that then.

9 MR. KIRBY: I think we have to start with the question  
10 of what does the statute say, and reach some kind of common  
11 understanding as to what the statute says, because the  
12 trustee's fundamental argument is that, whatever the statute  
13 says, SIPA somehow unwinds that or undoes that. And I think  
14 there are some important statutory provisions that your Honor  
15 addressed in the *Greiff* decision that I think we would request  
16 that you revisit because of some statutory provisions that were  
17 not argued by the parties in that case and were not presented  
18 to the Court as far as we are aware.

19 Let me start with the provision of Section 8(c)(3) of  
20 the SIPA statute, which the trustee argues alters the trustee's  
21 bankruptcy avoidance powers and deprives a customer of remedies  
22 that in our view Congress went out of its way to preserve.

23 Our view is that the plain language of the bankruptcy  
24 statute preserves all of the value defenses in Section 548(c).  
25 That's because SIPA borrows from the bankruptcy statute for

1 purposes of avoidance actions, and therefore we need to first  
2 look at the bankruptcy code.

3 What I would ask the Court to do is indulge us, is  
4 that there are several provisions of the statute which we refer  
5 to and I would like to discuss with the Court, and if I may,  
6 with your permission, we have prepared a compendium of key  
7 provisions in the statute which I would like to discuss.

8 THE COURT: Sure. But so far I am not hearing  
9 anything that wasn't fully in your brief. It's not going to be  
10 a good use of your time to just repeat to me what I have  
11 already read in your brief. And you can do that if you'd like,  
12 because if I look around this large bench, I'm sure I can find  
13 some other good work that I can do while you're doing that.

14 MR. KIRBY: Let me come right to the point about what  
15 we believe needs to be revisited with respect to the question  
16 of the SIPA statute, and I would offer these provisions of the  
17 code to look at so that we can look at them together, because  
18 some of these were not discussed in your Honor's decision.

19 THE COURT: Hand them up. It's not a question of what  
20 was discussed in my decision. It's a question of what was  
21 discussed in your brief.

22 MR. KIRBY: I would like to start with tab 11, Section  
23 6(b). We have highlighted the provision. I have provided this  
24 to counsel. It says, "Application of Title 11," and it says,  
25 "To the extent consistent with the provisions of this chapter,



1 a liquidation proceeding shall be conducted in accordance with  
2 and as though they were being conducted under chapters 1, 3 and  
3 5 and subchapters 1 and 2 of chapter 7." What the statute does  
4 is it incorporates the provisions of chapter 5 of the  
5 bankruptcy code into the SIPA statute for purposes of decision.

6 I would also like to refer the Court to tab 12, which  
7 is the provision of 7(a) which the Court did address in the  
8 *Greiff* decision. It says, "The trustee shall be vested with  
9 respect to the debtor and the property of the debtor, including  
10 the same rights to avoid preferences as the trustee indicates  
11 under Title 11."

12 Now, what I would like your Honor to focus on is the  
13 provision in tab 2, which is the definition of property of the  
14 estate. In tab 2 it says, "The commencement of a case under  
15 Title 11 creates an estate, and such estate is comprised of all  
16 of the following property, wherever located and by whomever  
17 held." Then it's 3. "Any interest in property recovered under  
18 Section 550."

19 So what does the bankruptcy statute do? It takes  
20 property recovered and makes it part of the general estate.

21 It is with that understanding, because SIPA has now  
22 borrowed those provisions, that's how you have to then turn to  
23 what the statute says in Section 8(c)(3).

24 That's a provision that this Court spent some time  
25 discussing in your Honor's decision. Let's look at the

1 language. It says, "Whenever customer property is not  
2 sufficient," and so forth, "the trustee may recover any  
3 property transferred by the debtor which, except for such  
4 transfer, would have been customer property if," and it says,  
5 "if and to the extent such transfer is voidable or void under  
6 the provisions of Title 11."

7 The next sentence says, "Such recovered property shall  
8 be treated as customer property."

9 Now, why is that there, your Honor? They had to write  
10 that in the statute because in section 6, they have made the  
11 provisions of chapter 5 and the definition of property of the  
12 estate. And so they had to undo that with respect to what  
13 bucket of property would be -- how the customer property would  
14 be treated in the event that they recovered that. They had to  
15 create a special statutory provision to undo the provision that  
16 is set out in section 6. That's all that that provision does.  
17 We think it is not appropriate to read that provision as  
18 altering the avoidance provisions of the bankruptcy code,  
19 because let's go back to what the bankruptcy code allows.

20 It is our view, and if you read our brief you're very  
21 familiar with that, that -- let me give you an example of what  
22 we are talking about. I am a Madoff customer and in the year  
23 2000 our client invests \$100. In 2007, our client withdraws  
24 \$200. Under the trustee's methodology, he sues our client for  
25 the \$100. But on what the statute says, the value defense

1 says, given the tort remedies that we have, is that under New  
2 York law, we were entitled to 9 percent interest for seven  
3 years, and the statute says, Section 548(c) says, we may retain  
4 that amount. So what that means is that we may retain that  
5 amount, and, therefore, what we are asking for is that our  
6 client would be entitled to keep, nine times seven is 63 under  
7 New York statutory interest.

8 THE COURT: I thought the 9 percent was on debt  
9 certain or judgments of law and things like that.

10 MR. KIRBY: That's not what the New York statute says,  
11 your Honor. The New York Court of Appeals has clarified that  
12 in the *Republic of Argentina* case. And in that respect, the  
13 trustee cites the *Bayou* decision in the district court, and  
14 that court says under New York law that is not speculative. In  
15 fact, the New York courts have clarified in the *Republic of*  
16 *Argentina* case, which we cite in our papers, that interest is  
17 mandatory, and that under New York law interest is mandatory  
18 from the date when a person defrauds a person and induces them  
19 to part with their money until the date when that money is  
20 returned. That's New York statutory law.

21 Federal law is to the same effect. The federal  
22 statute, which is the federal law in the *Randall v.*  
23 *Loftsgaarden* case by the Supreme Court, they incorporated the  
24 provisions of 12(a)(2) and recognized that a federal rescission  
25 remedy is available to a party. With respect to a rescission

1 claim, they are not only entitled to consideration paid, which  
2 is the principal, but interest thereon. That's what the  
3 statute says.

4 So the question is, why would Congress have altered  
5 that in anything in SIPA? It doesn't. It doesn't. In fact,  
6 Section 28(a) of the 34 Act, which is the rule of construction,  
7 and Section 2 of SIPA, which is the provision of SIPA that says  
8 that the SIPA provision is part of the 1934 Act, that rule of  
9 construction is very specific, and that is, it preserves any  
10 and all additional remedies at law and in equity. That  
11 provision is in our statutory appendix.

12 So what we are saying here is --

13 THE COURT: I must say I saw that in your brief  
14 repeatedly. I am not quite sure I understand the significance  
15 of it. Congress in enacting the 1934 Act and providing certain  
16 remedies there said, of course, all the other remedies that are  
17 out there still exist. I don't see how that translates into  
18 something about how you characterize something like a claim for  
19 interest here. Either you have that claim under New York law  
20 and it's not overwritten by federal law or you don't. But that  
21 would be true regardless of whether that provision was in the  
22 34 Act or not.

23 MR. KIRBY: Well, absent that rule of construction,  
24 because the federal statute gives you, as it's now interpreted,  
25 you both have the remedy under Section 29(b) of the statute,

1 which is the rescission remedy, the federal rescission remedy  
2 in the 34 Act, and you have the implied remedy under 10b-5.  
3 Both of those have been interpreted to say that not only do you  
4 get your rescission claim, but the rescission claim plus  
5 interest. That's the federal remedy. Then the question is,  
6 what did Congress intend, to preempt the state law or not?  
7 What we are saying in 28, and the cases are uniform on this, is  
8 that Congress is not intending to preempt that remedy --

9 THE COURT: But I thought your basic position on  
10 preemption was, unless Congress has made crystal clear that  
11 something is preempted, it's not preempted. So that has  
12 nothing to do with this catch-all business in the 34 Act. That  
13 is just window dressing.

14 MR. KIRBY: It actually does because that gives our  
15 clients the right to elect --

16 THE COURT: Would you say, in the absence of the 34  
17 Act provision, would your claim for interest, because that's  
18 what you're starting with, be preempted?

19 MR. KIRBY: If Congress was silent on that question?

20 THE COURT: Yes.

21 MR. KIRBY: I would say today and with the present  
22 Supreme Court, the answer would be no. But at the time when  
23 they wrote it in 1934 --

24 THE COURT: I am not sure what that answer means.

25 MR. KIRBY: It's important because the preemption law

1 has developed considerably over that, but whether there is an  
2 ambiguity or not as to the preemption law, Congress is crystal  
3 clear that you both have your state remedies and your federal  
4 remedies.

5 THE COURT: Go ahead.

6 MR. KIRBY: So what we are saying is that the value  
7 defense in Section 548(c), which is a defense that says you  
8 have a right to payment, an antecedent debt is a right to  
9 payment, and that is a defense to an avoidance claim.

10 Now, the trustee says this was all decided by the net  
11 equity decision, but it wasn't. Many of our clients did not  
12 submit claims here. But our clients are entitled to assert  
13 that defense as a right to payment in these avoidance actions.  
14 That's how it arises as an antecedent debt. And what the  
15 statute says is they may retain any right to payment as an  
16 antecedent debt that occurred at the time there was a transfer  
17 to our client.

18 So on my hypothetical, back to my \$100-\$200 example,  
19 when our client pulls out \$200, at that time they were entitled  
20 to interest on that money, at the New York statutory rate of 9  
21 percent for seven years, so they were entitled to \$163.  
22 Whether they are entitled to additional amounts, \$37, is a  
23 determination of whether they have additional claims of right,  
24 rights to payment under state or federal law. And we have set  
25 forth in our papers the basis for that. We are here

1 representing many defendants and each defendant should have a  
2 right to assert that.

3 THE COURT: None of whom, I think, invested just \$100.

4 Please continue.

5 MR. KIRBY: I used the example because the arithmetic  
6 was simple.

7 THE COURT: I understood that and with a dumb judge  
8 you have to do that.

9 Go ahead.

10 MR. KIRBY: What we are saying, in going back to that,  
11 is that this is a Rule 12 motion. On the face of the  
12 complaint, the trustee has admitted that there was a fraud,  
13 that each of our clients were induced to part with their money  
14 as part of a fraud, that each of our clients therefore -- that  
15 Madoff was a fiduciary. Our clients had a state law breach of  
16 fiduciary duty claim. They had a fraud claim under Rule 10b-5.  
17 They had a claim under Section 29 to undo that transaction,  
18 29(b) of the 34 Act. Those claims they have a right to assert  
19 as part of their defense. And the remedies that are available  
20 to them, that is the right to payment that the statute provides  
21 for. And that is what is preserved in Section 548(c) as their  
22 defense.

23 What the trustee has argued before is that somehow  
24 SIPA undoes that. But that's not what the SIPA statute says.  
25 The provisions we looked at says the trustee has the same

1 avoidance power as a bankruptcy trustee, and the provisions in  
2 Section 8(c)(3), which are the ones that your Honor addressed  
3 in the *Greiff* decision, says the trustee has the power if and  
4 to the extent the claim is void or voidable under the  
5 provisions of Title 11. And it is for that reason we say the  
6 powers of avoidance of a SIPA trustee are identical to the  
7 powers of a bankruptcy trustee and a bankruptcy trustee cannot  
8 avoid claims just ipso facto. They have a right to assert that  
9 defense and such other statutory defenses as they have as part  
10 of their antecedent debt defense. That's the position we are  
11 taking.

12 Now, I would like to turn, if I may, your Honor, to  
13 the second point in our papers, the effect of the obligation  
14 provisions in the statute.

15 THE COURT: Mr. Kirby, you are a very skilled  
16 attorney. Everything you say is well worth hearing. But you  
17 will forgive me if I say that I really think you're just  
18 repeating what is in your brief. It was well crafted in your  
19 brief. It's well-spoken here when you presented it orally. I  
20 appreciate hearing it again, but it's really not what I intend  
21 oral argument to be about. I guarantee you I have read your  
22 brief. I will go back before I decide this motion and read all  
23 the briefs and read them carefully again.

24 The reason I began this argument on the one issue that  
25 I felt perhaps had not been clarified in the briefs to my



1 satisfaction was just that. It well may be that there are  
2 other things that I have overlooked that have occurred to you  
3 in the interim since the briefing was completed in this case,  
4 and your adversary who didn't have the right of a reply paper  
5 may have even more along those lines, but that's what I get out  
6 of oral argument. It is hearing things that are new. So I  
7 apologize for limiting you in that way, but I'd really  
8 appreciate it if you would focus on things that are not in your  
9 papers that you want to bring to my attention.

10 MR. KIRBY: Your Honor, on the second point, which is  
11 the inter-account transfer obligations, where the trustee has  
12 not sought to avoid the obligations, I will rest on our papers  
13 in light of that, and I will turn the matter over to Mr. Schwed  
14 to address you on the new value.

15 THE COURT: Thanks very much.

16 Before we hear on that, let me hear from the trustee  
17 on the points that were just addressed.

18 MR. WARSHAVSKY: Your Honor, I think I would start at  
19 the statute, and I probably will only go to the statute. Mr.  
20 Kirby gave it to us. It's tab 13, 78fff-2. And Mr. Kirby  
21 highlighted for your Honor number 3. And that's a legal  
22 fiction which your Honor has written about but --

23 THE COURT: Where are you looking again?

24 MR. WARSHAVSKY: I am looking at 10 of 13. The  
25 statute is 78fff-2, on the second page of that.

1 THE COURT: Which of the tabs?

2 MR. WARSHAVSKY: Tab 13.

3 THE COURT: OK. I am now with you.

4 MR. WARSHAVSKY: 78fff-2(c)(3) is a legal fiction  
5 which your Honor has written about in various opinions at this  
6 point. But the one issue which I think is important to  
7 remember here is why the legal fiction operates this way, which  
8 is that this was not money -- throughout this case, it was  
9 always talked about that the money was theoretically in  
10 accounts that Madoff set up. And so, theoretically, Madoff  
11 never took title, as it were, to the money. The reason that  
12 the fiction is in place is so that customer property can be  
13 brought back into the estate. And it's all about customer  
14 property and adding back to the estate.

15 What Mr. Kirby didn't cite to -- let me take one step  
16 back. What 78fff-2(c)(3) is based upon is there being a  
17 shortfall in 78fff-2(c)(1). And by the terms of the statute,  
18 it says, "Whenever customer property is not sufficient to pay  
19 in full the claims set forth in subparagraphs (A) through (D)  
20 of paragraph (1), the trustee may recover any property  
21 transferred by the debtor," and it goes further.

22 If we turn now to 2(c)(1), it talks about the payment  
23 scheme, but what is important --

24 THE COURT: Just focusing back on what you were  
25 reading, "The trustee may recover any property transferred by

1 the debtor which, except for such transfer, would have been  
2 customer property if and to the extent that such transfer is  
3 void or voidable under the provisions of title 11."

4 So your adversary is saying this doesn't fall in that  
5 box.

6 MR. WARSHAVSKY: I didn't understand my adversary to  
7 be saying it doesn't fall in this box. Actually, I thought  
8 that's how he characterized all of our claims. What he said  
9 was that he has certain defenses by virtue of being a customer  
10 defrauded by Bernard Madoff.

11 THE COURT: That's right.

12 MR. WARSHAVSKY: That's where I turn to 2(c)(1), which  
13 has the allocation, which is on the same page at tab 13, right  
14 above the highlighted section.

15 THE COURT: I see.

16 MR. WARSHAVSKY: It's the section above. 2(c)(1)  
17 actually lists how the trustee is to allocate customer  
18 property. But what is important is the last paragraph there,  
19 which actually is all the precursor to 2(c)(3). This is  
20 2(c)(1). It says, "Any customer property remaining after  
21 allocation in accordance with this paragraph shall become part  
22 of the general estate of the debtor." We don't have that  
23 problem here. We are not getting to a general estate any time  
24 soon.

25 So then we turn to the next sentence. "To the extent

1 customer property and SIPC advances pursuant to 78fff-3(a) of  
2 this title are not sufficient to pay or otherwise satisfy in  
3 full the net equity claims of customers, such customers shall  
4 be entitled, to the extent only of their respective unsatisfied  
5 net equities, to participate in the general estate as unsecured  
6 creditors."

7 So that tells you when and how customers can  
8 participate in the general estate. Under 78fff-2(c)(3), the  
9 trustee is proceeding against Mr. Kirby's clients as customers.  
10 It is proceeding against customers who are the fund of customer  
11 property. To the extent that Mr. Kirby's clients have a claim  
12 back against the fund of customer property, and even against  
13 the general estate, it's limited specifically to their claims  
14 of net equity. I know. It's my favorite thing to bring up.  
15 But that's what their claim is circumscribed by.

16 If he wants to come forward later as a tort victim and  
17 sue the general estate, that's something separate. He may or  
18 may not have a claim. That's a factual issue. That's beyond  
19 this point. There is one case that we cited in our brief.  
20 There are two cases that we subsequently found. I shared them  
21 with my adversaries this morning. Both say the same thing,  
22 which is, and I am reading now, and I am happy to provide  
23 copies to chambers if you so like, but I am reading from *In re*  
24 *Government Securities Corp.*, which is bankruptcy court of  
25 Florida, the cite 90 B.R. 539. I am reading at page 542.

1 THE COURT: What is the year?

2 MR. WARSHAVSKY: 1988. There aren't that many cases.

3 What it says is about the creditors, "Each may or may  
4 not have a fraud claim should it ever become worthwhile for  
5 them to prove up such a claim as a general creditor, but none  
6 has an unsatisfied customer claim which can be enforced against  
7 the fund of customer property or against that fund as  
8 supplemented by SIPC." And we cite in our brief *In re MV*  
9 *Securities*, which is from the bankruptcy court in this district  
10 from 1985. These cases, and there is a different one from this  
11 district which is unpublished from 1975, but they all hold the  
12 same thing, which is that SIPA satisfies net equity claims, it  
13 doesn't satisfy fraud claims. A fraud claim can't be asserted.  
14 And I understand Mr. Kirby is suggesting it's a defense, but  
15 ultimately the inquiry that we have heard throughout today, and  
16 that appears throughout my adversary's papers, is what claim  
17 could they have asserted against the estate, where does  
18 interest start running, etc. It all has to do with these  
19 defendants' affirmative rights against the estate.

20 THE COURT: So your fundamental point is not that they  
21 don't have these claims, but that their claims are only  
22 assertable against the general estate, and that under the  
23 provision that you have just been referring to, a priority is  
24 given to the SIPC trustee with respect to not entitling them to  
25 make those claims if they go beyond their net equity.

1 MR. WARSHAVSKY: You said it more concisely than I  
2 did. That's my only response.

3 THE COURT: Go ahead.

4 MR. WARSHAVSKY: My one other response would be that  
5 ultimately I understand Mr. Kirby's argument that these  
6 defenses may be apparent from the pleadings, but all of them  
7 are laden with factual issues, and ultimately when there is a  
8 request for 9 percent, what ultimately seems to be 9 percent  
9 prejudgment interest, number one, I question whether the  
10 defendant is entitled to that in this court. I am not aware of  
11 every case issued by the Southern District, but I am not aware  
12 of 9 percent prejudgment interest being awarded.

13 THE COURT: You're wrong. That's quite standard.

14 MR. WARSHAVSKY: Is it? Then I have been unlucky, or  
15 maybe lucky as a defendant.

16 But ultimately that's at the end of the case. Much  
17 like an attorneys' fees clause or anything else, that is after  
18 the defendants have put on their proofs and actually won their  
19 case.

20 THE COURT: What he is saying is that's true when the  
21 actual award is made, but that doesn't mean you don't have a  
22 claim for it from the get-go. I think your first point may be  
23 stronger than your second point.

24 MR. WARSHAVSKY: Then I will leave with my first  
25 point.

1 THE COURT: Let me hear from the SIPC trustee.

2 MS. ATTARD: Thank you, your Honor.

3 I just want to correct some things about SIPA and  
4 about the bankruptcy code.

5 Mr. Kirby suggested that Section 541, property of the  
6 estate, in the bankruptcy code somehow refers only to a general  
7 estate in a SIPA liquidation. However, when we look at some of  
8 the provisions in SIPA, we see that property of the estate and  
9 property of the debtor are kind of used interchangeably and  
10 really refer to both the general estate and to the fund of  
11 customer property.

12 I want to just point out the definition of customer  
13 property is in Section 78111(4), and I don't believe it's in  
14 Mr. Kirby's compendium. I actually did not check.

15 THE COURT: That's all right. Go ahead.

16 MS. ATTARD: It says, "The term 'customer property'  
17 means cash and securities (except customer name securities  
18 delivered to the customer) at any time received, acquired, or  
19 held by or for the account of a debtor from or for the  
20 securities accounts of a customer, and the proceeds of any such  
21 property transferred by the debtor, including property  
22 unlawfully converted." And then it goes on and lists five  
23 subsections of additional customer property.

24 My point is the definition of customer property is  
25 incredibly broad and that these two estates really need to be

1 considered and thought of even in an avoidance action. Here,  
2 if the defendants give back these fictitious profits, every  
3 single dollar goes into the fund of customer property, every  
4 single dollar goes to the other victims of BLMIS, those who are  
5 the so-called net losers, those who have not yet received their  
6 principal back. So while it's easy to try to divorce avoidance  
7 actions from the claims process, I think it's very important to  
8 look at these two estates as a whole when considering Mr.  
9 Kirby's defenses and other points that he is raising.

10 THE COURT: All right.

11 Mr. Kirby, let me hear from you in response.

12 MR. KIRBY: I am going to start with the fact that our  
13 clients are not submitting claims in the SIPA case. So the  
14 only place that they can assert this defense is in response to  
15 the avoidance claim. The statute says that they have an  
16 antecedent debt defense. The statute doesn't say that's a  
17 junior claim or a senior claim. It says, if there was a debt  
18 that was due at the time of the transfer -- and remember what  
19 the language says in Section 548(c). It's probably worth  
20 focusing on the language because it says "may retain any  
21 interest transfer to the extent that such transferee gave value  
22 to the debtor in exchange for such transfer."

23 We said in our papers the time to decide that question  
24 is at the time of the transfer. They gave value as of that  
25 time because they had a tort claim for both the principal,



1 which the trustees conceded, and in addition, the tort claim to  
2 interest, and they had that at that time. At the time they  
3 received the transfer, they gave up, that was the exchange of  
4 value. What we said in our papers, we cited the cases that say  
5 the time to decide that question isn't sometime years later  
6 when there was a SIPA proceeding. Our clients don't have to  
7 submit a claim at this point. They have a right to assert that  
8 as a defense in the context of these proceedings.

9 And the definition of customer property for purposes  
10 of the avoidance provisions of the bankruptcy code is  
11 irrelevant because it says the trustee may avoid a transfer to  
12 the extent permitted by the bankruptcy code. As your Honor  
13 pointed out to Mr. Warshavsky, it says, "if and to the extent  
14 avoidable or void under Title 11." So the trustee doesn't have  
15 any greater avoidance powers in a SIPA case than any other  
16 bankruptcy trustee does.

17 So the only question is, our substantive statutory  
18 right to interest, and other claims that we have, where do  
19 those get asserted? We don't need to submit a claim in the  
20 bankruptcy case. We are not part of that case. They have sued  
21 our clients.

22 THE COURT: Doesn't your approach really undercut the  
23 whole point of the allocation priorities that your adversary  
24 was reading about before, that one of the points of SIPA  
25 legislation was to give customers a super priority in effect

1 and make them have their own champion in the form of the  
2 trustee, and enable them to get recoveries with a preference  
3 above others, and that is sort of spelled out in the language  
4 of 78fff-2(c)(1). And your approach would undercut that,  
5 wouldn't it?

6 MR. KIRBY: No, your Honor. You have to look at it  
7 this way. The SIPA process is designed to provide customers  
8 who have claims, and they set a priority scheme for those  
9 claims. Our clients don't have claims, many of them didn't  
10 even submit claims in the case. Some did, but many of our  
11 clients did not submit claims. They are not part of that case.  
12 The trustee has sued them, and we are saying he sues our  
13 clients, which are strangers to that case, as if they were  
14 suing anybody else. They then have such defenses as the  
15 bankruptcy statute provides for them. They are entitled to  
16 assert those defenses now because --

17 THE COURT: I understand that point. What I am not  
18 understanding is, if that point is carried out in the manner  
19 you say, which certainly has some support in some of the  
20 language of the provisions, but the statutes have to be read as  
21 a whole, and isn't the total effect of your approach to really  
22 undercut what the whole SIPA statute is designed to achieve?

23 MR. KIRBY: Your Honor, the answer to that is no.  
24 Otherwise why would Congress have said they have the same  
25 powers of avoidance as the bankruptcy trustee? They borrowed

1 that from the bankruptcy statute. Why would they have said in  
2 the provision that we are looking at, if and to the extent such  
3 property is void or voidable?

4 What it is saying is, the way I understand the  
5 statute, is if the trustee can avoid a transfer, he can recover  
6 it and put it in a bucket of customer property for distribution  
7 out. But our clients are entitled to assert as a defense any  
8 right to payment they had at the time of transfer. That's what  
9 the statute says. It borrows from the bankruptcy code in  
10 establishing that. That's what we are saying. And that's what  
11 the bankruptcy statute allows for.

12 As we have pointed out, there is this long line of  
13 Ponzi scheme cases that says, oh, well, that's somehow  
14 inequitable. But we are not dealing with that because there is  
15 no exception under 548(c) for Ponzi schemes. It doesn't say in  
16 548(c) except in Ponzi scheme cases. It's just not written  
17 into the statute.

18 THE COURT: I am sympathetic to the argument, though I  
19 am not making any rulings on anything right now, that courts  
20 cannot read in a "Ponzi scheme exception" to the literal  
21 language of the statute, even though, as you point out, there  
22 are quite a few courts that seem to have said that, but that  
23 seems to me to be arrogating to the courts a power that the  
24 courts don't possess.

25 But I have never understood that to be the trustee's

1 main point, though he occasionally throws it in. His main  
2 point, especially with regard to the issue that we are dealing  
3 with now, is that when you have multiple statutes --  
4 bankruptcy, securities, SIPA, which is kind of a hybrid, and  
5 others -- it is very much the role of the court to try to make  
6 them all gel together. And Congress does its best to make them  
7 gel, but Congress doesn't have perfect foreseeability and  
8 inevitably situations arise, of which Ponzi scheme situations  
9 are one example, where you have to see if there are ways to  
10 interpret the statutes collectively that makes sense, that is  
11 consistent with the congressional purpose.

12 That's precisely why I withdrew the reference because  
13 this did involve the interplay of bankruptcy and non-bankruptcy  
14 statutes in a situation that was by no means crystal clear  
15 under the case law, and I notice the trustee is always careful  
16 to preserve for appeal his opposition to my withdrawing the  
17 reference, but in fact the very arguments he makes in this very  
18 case show why withdrawal is mandatory. But that's the issue  
19 that you have to grapple with. It's an issue of making sure  
20 that all these things meld together in a way that makes sense.

21 So you are quite properly singling out the literal  
22 language of one or two provisions. That may be the end of the  
23 issue. I don't know. But I am not sure it's end of the issue  
24 because it seems to me to be contrary to the purposes of SIPA.

25 MR. KIRBY: Your Honor, this is why we referred to

1 what -- I understand that SIPA is part of the 1934 Act. Let me  
2 come back to that point because we raised that before. What  
3 SIPA says -- and remember the 34 Act has expansive fraud  
4 remedies and preserves the state law remedies that exist. It's  
5 in that backdrop that you need to read the avoidance  
6 provisions, which it would be very odd for Congress to say  
7 that, Oh, in enacting SIPA, we are going to undo those very  
8 fraud remedies that were recognized available to defendants in  
9 our situation. That would be an odd reading of the statute.

10 So what we say is that when Congress said that the  
11 same avoidance powers that's available to a bankruptcy trustee  
12 are available to a SIPC trustee, they meant that. And what  
13 that means is that we are entitled to assert debt value  
14 defenses that existed as at the time the transfers took place.  
15 Those defenses are preserved. We think that, based upon my  
16 example, on the face of the complaint, we can decide that  
17 question as a Rule 12 matter, at least part of it. But I think  
18 a square reading of the statute reconciles those purposes. It  
19 would be an odd reading of the statute, in our view, to say  
20 that these fraud remedies -- well, some of the fraud remedies  
21 are OK, we will give you principal. But when a federal statute  
22 says principal plus interest, the state statute says that, why  
23 should those be written out of the statute, especially when you  
24 find that Congress didn't by accident put SIPA into the 34 Act.  
25 They did it for a deliberate purpose. That's our point.

1 THE COURT: OK. Very good.

2 Does the trustee want to say anything further?

3 MR. WARSHAVSKY: Just one very small point, which is,  
4 if I am understanding Mr. Kirby correctly, and maybe he can  
5 answer this for your Honor, he is saying 2(c)(3) will never  
6 come into play, this legal fiction created by Congress will  
7 never come up.

8 The whole point of the fiction here is actually to  
9 take money withdrawn by a customer, and for this purpose only  
10 treat that customer as a creditor, and the end here says, "the  
11 laws of any state to the contrary notwithstanding." I wasn't  
12 sure what that last bit by Mr. Kirby meant. I do note that it  
13 does trump the state laws because the state laws are being  
14 relied upon here. But I am not clear from Mr. Kirby's last  
15 presentation where a trustee would ever be able to move under  
16 2(c)(3) if a customer could always come back and say that they  
17 were defrauded, they took money out of their account. This  
18 provision would be rendered moot.

19 THE COURT: All right.

20 Go ahead.

21 MR. KIRBY: I do want to respond to that point because  
22 there is a very obvious point in that last sentence of Section  
23 8(c)(3). It says, "For purposes of such recovery, the property  
24 to be so transferred shall be deemed to have been the property  
25 of the debtor and, if such transfer was made to a customer or

1 for his benefit, such customer should be a creditor, the laws  
2 of any state contrary notwithstanding."

3 What the purpose of that is is that there is a state  
4 law that says, when a customer submits money to a broker, that  
5 money belongs to the customer, and that's a bailment. In fact,  
6 our friends have argued this bailment theory for a long time as  
7 part of their standing point. But what this is saying, in  
8 those states where a customer would have a bailment right, that  
9 would not be property of the debtor, and they would not be a  
10 creditor because they are simply obtaining their own money.  
11 That is the reason why the Congress put in that last sentence  
12 of the statute. It wasn't intended to change the avoidance  
13 powers. The avoidance powers of the statute said, "if and to  
14 the extent void or voidable under Title 11."

15 So the way we read the statute is that if there is a  
16 shortfall in customer property, they can sue to recover that  
17 customer property, if and to the extent that it's void or  
18 voidable under Title 11, and when they recover that property,  
19 it can be put in the bucket of customer property. And what  
20 they are overwriting in the defense that the customer might  
21 make is that's not property of the debtor at all because it was  
22 my customer. That the Congress is clearly overwriting. So  
23 this statute, when you read it carefully, your Honor, is very  
24 precise on our rights and what the purpose of the statute was  
25 intended to do.

1 THE COURT: All right.

2 Well, it's, as all these questions, extremely  
3 interesting.

4 MS. ATTARD: I just want to clarify. I actually  
5 wasn't quite sure about what exactly Mr. Kirby was trying to  
6 say.

7 THE COURT: He is saying, as I understand it, with  
8 respect to the provision of (C)(3) in tab 13, it says that the  
9 trustee may recover any property transferred by the debtor  
10 which, except for such transfer, would have been customer  
11 property, if and to the extent that such transfer is void or  
12 voidable under the provisions of Title 11. He reads that  
13 language as saying that "if and to the extent that such  
14 transfer is void or voidable under the provisions of Title 11"  
15 means that if there are defenses that can be raised, they can  
16 be raised ab initio rather than, as the trustee was arguing,  
17 only being raised by making a claim against the general estate.  
18 That's the point I think he was making.

19 MS. ATTARD: I just want to clarify the last sentence.  
20 There is state law which says that preferences in fraudulent  
21 transfers cannot be recovered unless they are property of the  
22 debtor -- unless -- I am getting confused after all of this.

23 THE COURT: "For purposes of such recovery, the  
24 property so transferred shall be deemed to have been the  
25 property of the debtor and, if such transfer was made to a



1 customer or for his benefit, such customer shall be deemed to  
2 have been a creditor, the laws of any state to the contrary  
3 notwithstanding." He says all that means is that if there is a  
4 state law that would deem the property of the debtor to bear,  
5 it's the property of the creditor so far as that state law is  
6 concerned for these purposes.

7 MS. ATTARD: I think it's the other way around,  
8 because there are state laws which say that to recover it has  
9 to be property of the debtor and it has to be from a creditor.  
10 And here it's taking a customer and treating a customer as a  
11 creditor so that the trustee can recover from the creditor.

12 THE COURT: I see your point. OK.

13 MR. KIRBY: I agree with that reading.

14 THE COURT: OK. Good.

15 MR. WEINTRAUB: If I could just say very briefly that  
16 I think that the last sentence of (c)(3) is a red herring.

17 THE COURT: It's in yellow in the copy I have got.

18 MR. WEINTRAUB: Yellow herring.

19 I think the purpose of the deeming is just to  
20 correlate the language of SIPA which uses the term "customer  
21 property." The language of the bankruptcy code does not use  
22 that term but uses the terms "property of the estate" and  
23 "property of the debtor." It's just to let the trustee bring  
24 the avoiding action and the deeming is for purposes of having  
25 the avoiding action fit within the language of the bankruptcy

1 code. That doesn't have anything to do with the validity of  
2 the defenses that Mr. Kirby has been speaking about. That's a  
3 separate issue, your Honor.

4 THE COURT: All right. There was another issue that  
5 we were going to hear from counsel.

6 MR. SCHWED: Thank you, your Honor. Greg Schwed of  
7 Loeb & Loeb speaking on behalf of customer defendants who put  
8 new money into Madoff Securities during the two-year reach-back  
9 period, and I will try to observe the Court's injunction to not  
10 repeat matters that are in our briefs.

11 If I could be permitted just a second to return to the  
12 judge's dilemma on the issue you were just talking about,  
13 because I think perhaps another perspective in looking at how  
14 to square the circle here, it's a lot simpler than perhaps it  
15 may appear at first blush.

16 The net equity decision, made a decision about how to  
17 distribute property in a fund, and that's been decided by the  
18 Second Circuit and it's now fully the law.

19 The provisions that are under tab 13 that talk about  
20 how customer property is distributed and who gets a priority to  
21 that are very similar to the way property is distributed just  
22 in a garden variety bankruptcy case, where, for example, there  
23 are priorities for taxes, for unpaid wages, and they get paid  
24 first, and ultimately get down to just the general garden  
25 variety walking around unsecured claimants, and they get paid

1 pretty much last.

2 But that's entirely separate from the defenses that  
3 one can raise in a case. In a typical bankruptcy, a trustee  
4 can bring a lawsuit for fraudulent transfer and the defendant  
5 can say, OK, but I had an antecedent debt. And let's say it  
6 was just an unsecured debt, it was just a loan, but I was  
7 repaid a loan. That is a lay down, walk away defense to that  
8 case. And it makes no difference whether the trustee is  
9 representing a rich estate or a poor estate. It can be an  
10 estate with what is called an administrative deficiency, where  
11 they can't even pay enough money to pay the trustee or the  
12 lawyers. It doesn't make a difference. There has never been a  
13 case that said, well, if there is not enough money in the case  
14 to pay administrative claims or priority claims, then your  
15 defense of this plain old low priority unsecured claim is no  
16 good anymore. There is nothing in the statute. There is  
17 nothing in the case law that would suggest such a thing. And I  
18 think that's really the point that Mr. Kirby was making.

19 And Congress, despite it's well-publicized gridlock  
20 over the last few years, actually did do something intelligent  
21 in this statute, because they specifically deferred to a  
22 well-articulated bankruptcy code that's been around since well  
23 before the Bankruptcy Act of 1898 and was reformed in 1978.  
24 They didn't have to change the defenses. They knew what those  
25 defenses were, and they said it's good enough, and it's pretty

1 incandescently clear. "If and to the extent that such transfer  
2 is voidable or void under the provisions of Title 11." And  
3 Title 11 is the bankruptcy code, nothing to do with SIPA.

4 So it seems as if it's a simple reading of the  
5 statute. By all means the trustee should go out and get  
6 anything a regular trustee can get, and then the trustee  
7 distributes in accordance with the distribution pattern that is  
8 laid out here. But conflating the two is just wrong and it's  
9 not something that is contained in the statute.

10 THE COURT: So your point is that I really, in that  
11 little monologue I gave about having all these statutes work  
12 together, should have accused myself of creating a red herring  
13 because, at least as you read it, the SIPC trustee, while he is  
14 free to sue anyone that a trustee can sue, his special powers,  
15 if you will, relate to the distribution.

16 MR. SCHWED: Exactly, your Honor. That was the only  
17 supplemental point I wanted to make.

18 THE COURT: I understand.

19 MR. SCHWED: And again, mindful of the Court's warning  
20 not to repeat what is in our papers.

21 I did want to say that this issue that we specifically  
22 are focusing on is what happens when a good faith customer,  
23 someone where there has been no allegation of any wrongdoing,  
24 puts new money into Madoff Securities during the two-year  
25 reach-back period. And it's an issue of substantial importance

1 because this was, to the outside world, all good faith people,  
2 a very successful enterprise, and certainly customers would  
3 have been tempted to put money back in. So we don't have a  
4 quantification of the number. It's certainly not every  
5 defendant, but it's a lot of them.

6 It is a first impression issue, and I think that's  
7 important to point out. Obviously, skillful counsel, like the  
8 trustee in SIPC and hopefully us, try to make everything seem  
9 as if it couldn't be more clear, any fool can see that it has  
10 to be decided in our direction. But truth be told, no court,  
11 to our knowledge, has ever faced this issue before. And the  
12 reasons are probably fairly straightforward. Until the Madoff  
13 case, the idea of having a fraudulent scheme of this sort last  
14 not just for years, but for decades would have been  
15 inconceivable, let alone a fraudulent scheme that had this kind  
16 of visibility and patina of respectability to it. So because  
17 they typically don't last that long, it doesn't implicate a  
18 reach-back period at all. It sort of happens within six months  
19 or a year. So you have this strange effect, what do you do  
20 when somebody puts a million dollars or two million or \$100,000  
21 in during the two-year reach-back period?

22 What the trustee has said -- again, we think  
23 improperly extrapolated from the net equity decision, and it  
24 was narrowly crafted. This is the Court of Appeals. They are  
25 not going to decide something beyond what is in front of them.

1 THE COURT: They have been known to do that.

2 MR. SCHWED: I stand corrected. Although I think that  
3 they were trying to circumscribe it because it is a hornet's  
4 nest. There are a lot of issues bound up and this area of law  
5 is so far from seamless to not even be believable. So it just  
6 wasn't an issue in the case at all, nor was it in the Darnell  
7 case, which your Honor cited, quite properly, for the general  
8 rule. This is really a corollary of the general rule. It is  
9 an issue that the trustee says, well, there was a five page  
10 amicus brief that some defendants submitted after getting  
11 permission from your Honor in the *Katz* case. But the *Katz* case  
12 settled before the decision was actually made. I am sure that  
13 Mr. Warshavsky will say that this issue was decided in your  
14 Honor's decision in *Greiff*, but we don't think it was. We  
15 think the *Greiff* language can be easily modified to accommodate  
16 this special but important situation, because this issue was  
17 not argued at all, as far as we know, or discussed in *Greiff*.

18 And just in a nutshell, there are two ways really in  
19 which a new money investment can be handled. It can be handled  
20 in what we think is -- again, it's Occam's razor, the simplest  
21 way. You look at the money out and you subtract the money in,  
22 and there is the potential liability.

23 I should caution by saying, obviously we subscribe  
24 entirely to Mr. Kirby's argument that, in addition to the value  
25 of the money in, there would an increment as well for time

1 value of the money. But for the purposes of simplicity, I am  
2 just going to refer to it as the money out and the money in  
3 during the time frame that the trustee has a legitimate claim.

4 Now, the trustee in SIPC have appealed your Honor's  
5 decision on two years. We obviously think it is correct. We  
6 hope and think it will be affirmed in the Second Circuit. But  
7 it is certainly law of the case right now. What the trustee  
8 would do is say, well, I know you just put a million dollars  
9 in. Let's say you just take a simple example. You take out a  
10 million dollars, which is during two-year time frame.

11 THE COURT: You sure you don't want to deal with just  
12 \$100?

13 MR. SCHWED: In fact, your Honor, we put examples in  
14 our brief of customer A, customer B, customer C. I even have  
15 the charts here, if your Honor would like to go through them,  
16 to illustrate the illogical and we think absurd result and  
17 unfair result that would eventuate from using the trustee's  
18 method. Again, when you're in an area of this sort of terra  
19 incognita of first impression case, you sort of have to go the  
20 extra mile to think through, what is really the implication of  
21 this? And as we show in our illustration, we have a customer C  
22 who actually enriches the estate by putting significantly more  
23 money in during the two-year time period who ends up -- your  
24 Honor, if you would like --

25 THE COURT: I just wanted to have it here. There it

1 is.

2 MR. SCHWED: What we say is we set out three customers  
3 and tried not to make these implausible examples, but rather  
4 ones that fit a normal pattern. They all have the same  
5 beginning. Customer A, customer B, customer C, they all invest  
6 \$200,000 in 1988, which is not implausible. They take out  
7 \$400,000 in June of 2006, a date that was deliberately picked  
8 as being outside the two-year reach-back period.

9 Now, in some ways you would say, golly, these guys  
10 doubled their money, but they doubled it over 18 years so that  
11 was a 4 percent compounded return, which in that time period  
12 was not extortionate; that would have been certainly a fair use  
13 of the money. In any event, the double line after the third  
14 column is chronologically showing the two-year reach-back  
15 period. So anything after that black line is withdrawals.

16 So, again, all three of these customers then -- now  
17 it's live, they can be sued by the trustee under the Court's  
18 two-year decision. And each of them gets \$50,000. We are just  
19 going to assume that that is an absolute incontestable voidable  
20 claim.

21 Customer A puts the money back in, for whatever  
22 reason, puts it back in \$50,000, and nothing else happens.  
23 Those are the only transactions that occur with customer A.  
24 The effect on the estate during the reach-back period, which is  
25 the only period where there are live claims available, is there



1 is no effect; he or she got money out, put money back in, no  
2 effect. And under what we call the replenishment credit  
3 theory, there would be no liability.

4 Under the trustee's calculation, you go right back to  
5 the beginning of time and you say, well, these guys were  
6 \$200,000 overdrawn; therefore, the \$50,000 that they put in  
7 just gets swept up in the moor of that unrecoverable transfer  
8 and they can't use it. And we think that's just an indirect  
9 way of doing what they can't do directly, which is recover a  
10 time-barred claim. They could not go after that \$200,000, even  
11 it was \$2 million, but they are now using it to vitiate a  
12 credit that would normally be available for a customer who  
13 replenished the estate.

14 Now, the anomaly starts to come up when you look at  
15 what happens with customer B. Customer B is exactly the same,  
16 \$200,000 in, 400,000 out, so they are withdrawn but not  
17 vulnerable for 200,000, and then takes out a \$50,000 amount  
18 that is live and actionable. This defendant puts nothing back  
19 in.

20 THE COURT: But he is still liable for the same amount  
21 under their approach.

22 MR. SCHWED: Exactly. Under our approach, we say, no,  
23 there is no reinvestment of new money, so that defendant has to  
24 repay that money back, which makes sense.

25 The unfairness and absurdity sort of reaches a fever

1 pitch with customer C. The math is a little more complicated,  
2 but I think it's followable. Again, the same baseline facts.  
3 200,000 in, 400,000 out, not actionable. 50,000 is the first  
4 transaction that's actionable. Now, this defendant deposits  
5 \$100,000 of new money, very enthusiastic about Madoff  
6 Securities. Then has to take out \$100,000 to buy a house or  
7 education or whatever the purpose is. So takes out another  
8 100,000, and then deposits another \$100,000. So if you total  
9 that up, and I confess I will probably fail in trying to do it,  
10 but if you total up the total amount that is in and that is out  
11 within the two-year period, the estate actually is enriched by  
12 \$50,000. The estate got more than what the defendant took out.

13 Again, this has nothing to do with a claim in the  
14 case. We are not saying that this defendant would be entitled  
15 to a claim in the case. That's ancient history. It's just a  
16 minor demarcation between those two concepts, the distribution  
17 of assets from a limited fund, which the trustee has the right  
18 and SIPC has a right to call a claim on and defenses under a  
19 bankruptcy code in which that statute refers. But I digressed.

20 Under our replenishment credit theory, this customer C  
21 who enriched the estate by \$50,000 would have no liability.  
22 But under the trustee's method, the customer would be liable  
23 for \$150,000, three times as much as any of the other two, and  
24 bizarrely through the looking glass and for a defendant to  
25 actually put money into the estate during the live period.

1 THE COURT: What I don't know, and maybe the trustee  
2 can help me out, is under virtually any approach that one takes  
3 of this kind of situation, there are going to be unfair  
4 results, and even arguably weird results. The question is,  
5 among other things, would your approach lead to some weird  
6 results too? Obviously, not on your chart, but could be on  
7 their hypothetical chart. Because while this is very, very  
8 well done and very interesting, I think there is no way, no way  
9 that any court can fashion a series of rules applying to this  
10 kind of situation that will not be unfair in many given  
11 individual circumstances. Because in the end it's victims  
12 against victims. That's what it really comes down to.

13 So I didn't mean to cut you off, but I am anxious to  
14 hear from the trustee.

15 MR. SCHWED: If I could just respond?

16 THE COURT: Yes.

17 MR. SCHWED: I think your Honor is obviously correct.  
18 The most stark example of an unfairness that comes about is  
19 think of a customer who got \$20 million more than a customer  
20 put in, but it was one day before the two years, and somebody  
21 else who got that \$20 million one day within the statute of  
22 limitations. In one case the customer has got to give it all  
23 back. In the other case they put the money in their Cayman  
24 account and sail off. And to the layperson, and even to us as  
25 lawyers, it has sort of an unfair feeling, but it's really an

1 inherent part of the statute of limitations, or any limitations  
2 period. And we cite cases that say the policies of  
3 predictability are really based into our legal system, and we  
4 cite a Supreme Court case that talks about them and an early  
5 bankruptcy code case that says that this is just the way it is.

6 THE COURT: Predictability needs to be seen from the  
7 standpoint here of what Congress intended. If you just take an  
8 everyday avoidance action, from the standpoint of an innocent  
9 person who has money that they thought was theirs, for example,  
10 for their children's education or something like that, caring  
11 for their widowed mother, one could go on, and then lo and  
12 behold, it's grabbed back under everyday bankruptcy avoidance,  
13 and they are saying, gee, that's terribly unfair. And here is  
14 this guy who two years earlier did the same thing and he is not  
15 getting anything happen to him. So the predictability has to  
16 be, I think, looked at in terms of congressional intent here,  
17 not what the customer viewed as predictability, because no  
18 customer viewed it as predictable that they were going to have  
19 that money grabbed back from them even a week later.

20 Anyway, I take your point. Although I suppose, since  
21 we are talking about money spent on widows and education, there  
22 is also the guy who said, boy, I really need a third yacht, I  
23 am going to withdraw my money right now.

24 Anyway, let me hear from the trustee. Thank you.

25 MR. WARSHAVSKY: Your Honor, I think your response

1 actually hit upon what the trustee's would be, which is that  
2 ultimately what we are looking at here is a transaction -- we  
3 try to take, and I know everyone makes fun of us for this, and  
4 I have certainly taken a few shots today, but ultimately we try  
5 to take one consistent approach throughout and treat every  
6 customer who invested the same. The only way we can do that is  
7 by reconciling each account, money in, money out. What we have  
8 heard from the defense here throughout the day are various  
9 different iterations of how to keep the money, how to limit the  
10 trustee's ability to get that money back, not all of which are  
11 necessarily consistent with each other, but the result is that  
12 it would result in a variety of different rules.

13 So just here I am not sure what types of rules would  
14 be fashioned based upon the chart on page 30 of defendant's  
15 briefs. What happens if a different defendant comes in and  
16 just deposited \$10 million ahead of time and is only taking  
17 money out in the two-year period. Do we reset that defendant  
18 too or do we give him the credit for the 10 million in  
19 principal? The trustee's methodology has always been  
20 principal. The idea being, notwithstanding some of what Mr.  
21 Kirby said earlier, the fundamental precept that everybody was  
22 putting their money in to what was inherently risky, what we  
23 would try to give them back is their capital, but didn't have a  
24 right to make money. They certainly had that expectation, it  
25 may have been reasonable, but they didn't have a right to make

1 that money.

2 And so what we tried to do is say, let's give them  
3 their money back. How do we treat all customers, whether they  
4 won or they lost, in terms of net equity, perhaps they are all  
5 really losers here, how do we treat them as fairly as possible?  
6 What is a single methodology that can work across all of them?  
7 How do we factor in somebody who -- I guess it's a rhetorical  
8 question, but how could the trustee ever adopt a methodology to  
9 treat thousands and thousands of victims differently? We  
10 couldn't. It wouldn't be legally tenable and there would be no  
11 way to enforce it, and this case would take even longer. The  
12 result is that there has to be one methodology; we can't go  
13 with different methodologies.

14 In terms of what is now called the replenishment  
15 credit methodology, I do think we did see that in the  
16 *Katz/Wilpon* case where there was the amicus briefing. I do  
17 think it was briefed in *Greiff*. It was then called reset to  
18 zero methodology where new money was treated differently than  
19 old money. And ultimately that's really what Mr. Schwed is  
20 asking.

21 THE COURT: I may in the end be persuaded by your  
22 basic approach. I don't think that you should rely on whether  
23 it's being implicitly decided in *Katz*, where there was very  
24 limited briefing, or *Greiff*, where there was no briefing. Even  
25 law of the case can be changed by a judge if he, after

1 receiving new briefing, is persuaded he was in error. So  
2 you're right to raise those points, but I wouldn't get too  
3 optimistic about that. I think I am going to reach the merits,  
4 so to speak.

5 MR. WARSHAVSKY: Right. I rose those cases in that  
6 briefing just to raise the point that, while we have changed  
7 the name, ultimately the position that we have tried to adopt  
8 is that money deposited, whether it's in 1996, 1998, 2000,  
9 2004, 2006, or 2007 as in this example, is treated the same.

10 THE COURT: I understand your point.

11 MR. WARSHAVSKY: I would like to, because Mr. Schwed  
12 did go back to the last point, I would just like to say that  
13 notwithstanding what I thought was a very nice way of trying to  
14 frame the issue, neither he and, frankly, nor Mr. Kirby do  
15 address the point that, first of all, 78fff-2(c)(3) is absent  
16 from a typical bankruptcy --

17 THE COURT: I think we all agree that whoever codified  
18 this should be shot.

19 MR. WARSHAVSKY: Certainly the numbering system. Just  
20 that under the theory being proposed is rendered toothless  
21 here; the trustee wouldn't be able to avoid any of these  
22 transfers and bring back any money into the estate without it.

23 THE COURT: All right. Anything further?

24 MS. ATTARD: If I may, your Honor?

25 THE COURT: Absolutely.

1 MS. ATTARD: Just about Mr. Schwed going back in his  
2 elegant solution. I think it does ignore one key difference  
3 between the bankruptcy code and SIPA, which is that under the  
4 bankruptcy code there is one estate and in SIPA there are two  
5 estates. So we can see Section 78fff(d) is apportionment, and  
6 under that section of SIPA the trustee is directed as to which  
7 assets go to the general estate and which assets go to the fund  
8 of customer property. Unfortunately, under Mr. Schwed's  
9 solution, it ignores that critical fact.

10 THE COURT: Please.

11 MR. SCHWED: Mr. Warshavsky in his first comment  
12 seemed to suggest that somehow the approach we are suggesting  
13 would involve a hybrid approach or disparate treatment of  
14 customers, and he used the example, well, what about somebody  
15 who deposits \$10 million a day before the two-year time period,  
16 what happens to that customer? We deal with that in the brief.  
17 It is the essence of simplicity. It's an antecedent debt that  
18 that customer is entitled to assert against voidable transfers,  
19 just as in any garden variety bankruptcy case. It's not time  
20 limited. There is nothing in the statute that suggests it,  
21 nothing in the case law that suggests it. And so it's not a  
22 special pleading or some special rule, it's just what the  
23 bankruptcy code absolutely, incandescently provides.

24 All of the trustees' arguments is that there has to be  
25 one methodology. That's nice, but that's really not what the



1 statutes say. It's not even what the Court said in the *Greiff*  
2 case, where the Court said that, essentially, the statute of  
3 limitations can't all yield to the trustee's notion. However  
4 well-intended that everybody should be treated equally, there  
5 are statutory restraints; they are not always conclusively  
6 clear, but I think in this case they are.

7 So, again, the statement that somehow by adopting this  
8 view the trustee couldn't bring any money, it was rendered  
9 toothless, is just silly. The trustee can sue just like any  
10 other trustee can sue for fraudulent transfers, and all the  
11 defendants can assert their defenses. Whether they are  
12 effective or not is another question, but he just can't  
13 conflate the recovery system and say, well, because the net  
14 equity decision said that the transfers will be distributed in  
15 this way, somehow that attaches to the defenses to which SIPA  
16 expressly defers.

17 THE COURT: All right. Thank you very much.

18 All right. Now, I have also, when we set up this  
19 procedure of collective briefing and collective argument,  
20 provided that if there is anyone here, any lawyer here in the  
21 audience representing a party who wants to be heard on  
22 something that hasn't been argued, that opportunity is now.  
23 But I am delighted to see there are no takers.

24 I thank all counsel very much for this very helpful  
25 argument.